No. 15915

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of the Properties
MOULIN ROUGE, INC., a corporation and successor in interest to MOULIN ROUGE, a limited partnership,

Bankrupt.

In the Matter of
MOULIN ROUGE, a Limited Partnership,

Bankrupt.

ROSEHEDGE CORPORATION, a corporation,

Appellant,

vs.

MILLIE STERETT,

Appellee.

APPELLEE'S OPENING BRIEF.

ARTHUR N. GREENBERG,
6505 Wilshire Boulevard,
Los Angeles 48, California,
Attorney for Appellee.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.

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APPELLEE'S OPENING BRIEF.

Statement of the Case.

A. The Parties.

Appellee is a secured creditor of Moulin Rouge, a limited partnership, bankrupt, under a chattel mortgage of certain personal property situated in the Moulin Rouge Hotel, Las Vegas, Nevada, which mortgage was executed July 5, 1955 and recorded July 13, 1955 to secure a promissory note in the amount of $35,000.00. [R. 11-12, 21-29.]

Appellant also claimed to be a secured creditor of said bankrupt by virtue of a $195,000.00 loan secured by

(a) an assignment and pledge of a certain $600,000.00 Edna Shulman promissory note, (b) an assignment and pledge of a deed of trust securing said Edna Shulman promissory note on the land upon which the Hotel Moulin Rouge was subsequently erected, both of which promissory note and deed of trust were subject to a prior assignment and pledge to Leroy Investment Company, Inc., a California corporation, hereafter referred to as "Leroy", and (c) a chattel mortgage dated May 24, 1954 and recorded May 25, 1955 on substantially the same personal property which is the subject of appellee's chattel mortgage. [R. 10-11.]

B. Foreclosure Proceedings.

Upon the bankrupt's default in payment of the promissory notes in favor of appellant and Leroy, said parties commenced foreclosure actions against the Moulin Rouge realty on their respective pledges of the Edna Shulman promissory note and deed of trust. *No action was taken to foreclose appellant's chattel mortgage.**

On October 19, 1955, said Moulin Rouge, a limited partnership, commenced proceedings under Chapter XI of the Bankruptcy Act. Thereafter, the referee in bankruptcy stayed the pending foreclosure actions. [R. 91-92.]

On January 17, 1956, appellant and Leroy filed motions for leave to proceed with sale under the Edna Shulman pledge and trust deed. After hearings on objections thereto, the matter was submitted to the referee for decision. [R. 92.]

Thereafter, the trustee in bankruptcy petitioned the referee for authority to sell the real property encumbered

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*All emphasis in this brief is added.

by the Edna Shulman deed of trust "free and clear of all liens." Appellant and Leroy objected to said petition unless a stipulation proposed by them was approved by the referee. Subsequently on July 6, 1956, the referee granted the trustee's petition, approved and incorporated said stipulation into the order and directed the sale of the real property, including "the furniture, fixtures and other personal property contained therein. . . ." [R. 3-7, 99-102.]

Appellant and Leroy had informed both the referee and the trustee in bankruptcy that *they desired to bid at any sale and to utilize the value of their lien claims upon such bids and in payment of the purchase price if they were successful bidders.* [R. 97.] In accordance with this desire, the stipulation provided that upon the trustee's sale, appellant and Leroy, jointly and severally, could bid and become the purchaser thereof, and that they were entitled to use on account of such bids the amount of their respective claimed indebtedness. [R. 60.]

The stipulation further provided that appellant and Leroy had the right to include, principal, interest, attorneys' fees and all sums paid out or incurred by them, or either of them, for the protection or preservation of said real property "as a credit upon, and as payment upon the said purchase price of the property purchased." [R. 60-61.]

C. The Sale.

The trustee's sale took place on September 6, 1957 in accordance with the provisions of the referee's order of July 6, 1956. Appellant and Leroy were the highest bidders. For convenience, the bid was made in the name of S. Kohn, a secretary in the office of Mr. Katz, at-

torney for appellant and Leroy. However, the bid was in fact the bid of appellant and Leroy and was regarded by all parties and the referee as such. [R. 110-111, 117-118, 121-122.]

At the time the referee accepted said bid, he granted the motion of appellant and Leroy for leave to proceed with their sale under the Edna Shulman pledge and trust deed, and he also upheld the validity of the claims of appellant and Leroy as first liens against the real property of bankrupt. [R. 37-44.]

In announcing the bid, the attorney for appellant and Leroy stated:

> *"We do have an offer that we desire to submit, and our offer is, in effect, to pay the equivalent of roughly five hundred sixty or six hundred thousand dollars,* and the reason I say roughly is because the exact amount would follow the court's determination of what fees would be allowed on these in connection with the foreclosure of the trust deed, and that would be made up as follows. . . ." [Tr. of Sept. 6, 1957, p. 10.]

During the proceedings, the referee stated:

> "There is a lot of technical terminology that might not be clear when you hear it read. *What the offer in essence is is that Mr. Katz is bidding in the trust deeds held by Rosehedge* (appellant) *and Leroy, and he also is paying an additional one hundred sixteen thousand.* That one hundred sixteen thousand will go to pay expenses of administration." [Tr. of Sept. 6, 1957, p. 15.]

The referee stated at the sale and found that appellant and Leroy bid in the amount of the encumbrances held by them plus an additional $116,000.00. [R. 117-118, 120; Tr. of Sept. 6, 1957, p. 15.]

The referee's above findings in this respect are contained in his Certificate on Petitions for Review as follows:

> "It appears that under the Stipulation of June 19, 1956, and the Referee's Order of July 6, 1956, *Leroy and Rosehedge* (appellant) *were permitted to utilize, in whole or in part, the amount of their lien claims in connection with any bid made by them, or purchase price to be paid by them.* The bid by Mr. Katz on September 6, 1957, in the name of S. Kohn was announced as, and, in fact, was the bid of and on behalf of Leroy and Rosehedge, and was so considered and treated by the Referee, and all persons present at said sale. This bid was made subject to the liens and claims of Leroy and Rosehedge. *This, in the opinion, of the Referee, at the time of sale, was the equivalent of utilizing the value of the Leroy and Rosehedge claims upon the bid made.* Had the bid been increased by the value of such lien claims, a credit upon the purchase price in the amount of the value of the said lien claim would have had to be given. Such procedure would have been a useless and idle act." [R. 117.]

At no time did appellant object to the manner in which the referee regarded said bid and no petition for review of any referee's order was filed by appellant.

The principal asset of the bankrupt was the land encumbered by the $600,000.00 Edna Shulman deed of trust and the Hotel Moulin Rouge erected thereon. [R. 96.]

The record does not reflect the exact value of the land and the Hotel Moulin Rouge at the time of the bid. However, the liabilities of the bankrupt exceeded $2,100,000.00 to secured and unsecured creditors, and the sale to appellant and Leroy reduced by more than $820,-

000.00 the amount of lien claims, exclusive of chattel mortgages and conditional sales contracts. [R. 3-20, 93-94.]

At the time of the sale, appellant and Leroy bid in the sum of $116,000.00 plus the amount of their respective liens. The principal of appellant's loan had been reduced to $126,928.66 and its total lien claim including interest, costs and attorneys' fees, was $154,846.65. The total sum claimed by Leroy, including interest, costs and attorneys' fees was $272,722.50 and the total of both lien claims was $427,569.15. [R. 37-41.]

Thus, appellant and Leroy acquired the Hotel Moulin Rouge, and the land upon which it was situated, the principal asset of the bankrupt, for less than 25% of the bankrupt's outstanding indebtedness, of which the greatest part of their bid was used in satisfaction of their own secured liens. As a result, of all secured and unsecured creditors of bankrupt, only two were satisfied in full—appellant and Leroy.

Although both the referee and appellant regarded the bid as utilizing the entire amount of appellant's lien claim, the referee made no finding with reference to appellant's chattel mortgage of record, which was additional security for appellant's claimed indebtedness.

D. First Petition for Review.

Appellee joined in the filing of a petition for review of the referee's order of September 6, 1957 and principally urged that the referee's failure to act in respect of appellant's chattel mortgage had prejudiced her. [R. 50-56.]

E. Confirmation of Sale.

On September 23, 1957, the referee confirmed the sale to appellant and Leroy, ordering conveyance of the bankrupt's real property and personal property, subject to all

valid and subsisting conditional sales contracts and chattel mortgages. The referee did not specifically rule upon the ground in appellee's petition for review that her chattel mortgage was superior to that of appellant. [R. 66-75.]

F. Second Petition for Review.

Appellee then petitioned for review of the referee's order of September 23, 1957, incorporating by reference her earlier petition for review and realleging her earlier contention with respect to appellant's chattel mortgage. [R. 75-81.]

G. The District Court.

At the hearing before the District Court, it was urged that appellant's claim had been satisfied in full by utilizing the amount of said claim in making the bid on the real property, and that although appellant's claim was doubly collateralized, it was entitled to only one satisfaction and thus had no further claim under its chattel mortgage. [R. 124-127.]

Although the District Court dismissed appellee's petition for review, denied the relief sought by her therein, and overruled each of appellee's objections to the referee's order, it nevertheless ordered appellant to deposit in escrow a release of its chattel mortgage without prejudice to the rights of appellant to assert any claims or defenses, against appellee's chattel mortgage, except the claim of priority. Thus, the District Court impliedly found that appellant had bid in at the sale the amount of its lien claim, that its claimed indebtedness had been extinguished and that accordingly appellant had no further rights under its chattel mortgage. [R. 135-136.]

From the portion of the order requiring appellant to deposit a release of its chattel mortgage in escrow, this appeal has been brought. [R. 139-140.]

Summary of Argument.

1. The District Court ruled properly in ordering appellant to release its chattel mortgage through escrow because appellant's lien claim was satisfied and extinguished by utilizing the entire value of said claim in its bid for the bankrupt's real property.

2. The District Court had jurisdiction to order appellant to release its chattel mortgage through escrow.

I.

The District Court Ruled Properly in Ordering Appellant to Release Its Chattel Mortgage Through Escrow Because Appellant's Lien Claim Was Satisfied and Extinguished by Utilizing the Entire Value of Said Claim in Its Bid for the Bankrupt's Real Property.

A. The Evidence and Law Support the Order of the District Court.

The principal issue of this appeal is whether appellant's chattel mortgage lien claim has been satisfied and extinguished by reason of having utilized the entire value of its lien claim in its successful bid for the Moulin Rouge realty. If the entire value was utilized, then appellant's indebtedness was satisfied, its lien extinguished and the order of the District Court should be affirmed.

Appellant and Leroy were the assignees of a deed of trust, which constituted the first lien on the Moulin Rouge realty. [R. 37-44.] They were also the successful bidders at the sale of September 6, 1957 for the purchase of said real property.

Generally, the acquisition of mortgaged premises by the mortgagee results in a merger of the two estates, vesting the mortgagee with complete title, and ending his rights under the mortgage.

59 C. J. S. 672.

However, whether conveyance to a mortgagee of property covered by the mortgage results in merger of the fee and mortgage, is a question of the intention of the parties and depends upon the facts and circumstances of the particular case.

Guaranty Trust Co. of N. Y. v. Minneapolis & St. Louis R.R. Co., 36 F. 2d 747, 764 (8th Cir., 1929), cert. den., 281 U. S. 756;

Toston v. Utah Mortgage Loan Corp., 115 F. 2d 560, 562 (9th Cir., 1940);

59 C. J. S. 673, 677.

Contrary to the position taken by appellant in its opening brief, the evidence and the law clearly support the order of the District Court and its implied finding that appellant's lien claim was satisfied and extinguished by merger. The evidence is summarized as follows:

1. In announcing the bid of appellant and Leroy, the attorney for said parties stated as follows:

> *"We do have an offer that we desire to submit, and our offer is, in effect, to pay the equivalent of roughly five hundred sixty or six hundred thousand dollars,* and the reason I say roughly, is because the exact amount would follow the court's determination of what fees would be allowed on these in connection with the foreclosure of the trust deed, and that would be made up as follows. . . ." [Tr. of Sept. 6, 1957, p. 10.]

2. During the proceedings, the referee made it clear that appellant and Leroy were bidding in the full amount of their lien claims as follows:

> "There is a lot of technical terminology that might not be clear when you hear it read. *What the offer in essence is is that Mr. Katz is bidding in the trust deeds held by Rosehedge* (appellant) *and Leroy, and he also is paying an additional one hundred sixteen thousand.* That one hundred sixteen thousand will go to pay expenses of administration." [Tr. of Sept. 6, 1957, p. 15.]

3. Appellant and Leroy had both informed the referee and trustee in bankruptcy that they desired to bid at the sale and *to utilize the value of their lien claims upon such bids and in payment of the purchase price if they were the successful bidders.* [R. 97.]

4. The stipulation proposed by appellant and Leroy and incorporated in the referee's order of July 6, 1956, provided that appellant and Leroy could use the full amount of their claimed indebtedness as a credit and payment upon the purchase price of the real property of bankrupt. [R. 60-61.]

5. At no time did appellant attempt to foreclose or otherwise enforce its chattel mortgage. Its only action was relative to the bankrupt's real property.

6. There were no intervening liens on the real property or the Hotel Moulin Rouge, which constituted the principal asset of the bankrupt. The referee's order as confirmed by the District Court wiped out all other liens against said real property. Thus, appellant and Leroy acquired the principal asset of bankrupt free and clear of all liens. [R. 3-20, 33-49, 66-67.]

7. The value of the real property acquired by appellant and Leroy was greater than the amount of their combined claimed indebtedness, resulting in merger of the mortgage with the fee and extinguishment of the debt.

Central Hanover Bank v. Roslyn Estates, 42 N. Y. S. 2d 130 (1943), aff'd 293 N. Y. 680, 56 N. E. 2d 595.

The total lien claim of appellant and Leroy was $427,-569.15 including principal, interest, costs, and attorneys' fees. At the sale of September 6, 1957, appellant and Leroy acquired the principal asset of the bankrupt, namely, the Hotel Moulin Rouge and the land upon which it was erected. The land alone was encumbered by a $600,-000.00 deed of trust, which deed of trust was pledged and assigned to appellant and Leroy and bid in by them at the sale. The liabilities of bankrupt exceeded $2,100,000.00 to secured and unsecured creditors and the referee wiped out the rights of lien claimants of record, excluding chattel mortgages and conditional sales contracts, in excess of $820,000.00. Obviously, appellant and Leroy have obtained assets worth many times the amount of their combined lien claims. [R. 3-20, 37-41, 93-94, 96.]

It was argued to the District Court upon the hearing on the petitions for review that appellant was only entitled to be paid once although its claim was secured by both a chattel mortgage and a trust deed. [R. 124-127.] The District Court agreed and ordered appellant to release its chattel mortgage. The position of District Court is clearly supported by law.

The courts have uniformly held that a mortgagee is entitled to be paid in full *but is not entitled to receive more than the total amount of the mortgaged debt.*

Honeyman v. Jacobs, 306 U. S. 539, 542 (1939);

Gelfert v. National City Bank, 313 U. S. 221, 223 (1941).

In the *Honeyman* case, the United States Supreme Court stated on page 542 as follows:

> "The contract contemplated that the mortgagee should make itself whole, if necessary, out of the security, *but not that he should be enriched at the expense of the debtor or realize more than what would repay the debt with the costs and expenses of the suit."*

In *Guaranty Trust Co. of N. Y. v. Minneapolis & St. Louis R.R. Co.,* 36 F. 2d 747 (8th Cir., 1929), cert. den., 281 U. S. 756, cited by appellant in its opening brief, the court found that there was no merger by virtue of an express agreement between the parties. The court further stated on page 764 as follows:

> "Any other conclusion would work a manifest injustice to the Northern Pacific Company. *There is no claim that the property was worth more than the Northern Pacific paid for it.* It parted with its money, which it would lose to the junior lien holders, if they can now come in and assert priority of their liens."

It is obvious that to pay appellant twice would be manifestly unjust.

8. The referee found as a fact that appellant and Leroy utilized the value of their claims upon the bid made at the sale of September 6, 1957. [R. 117.]

Although said finding was not separately demarcated as such, it was set forth in the referee's certificate on petitions for review and had the full force and effect of a formal finding under Section 39(a)(8) of the Bankruptcy Act, 11 U. S. C. A., Sec. 67(a)(8), which provides that the referee shall:

> "Prepare promptly and transmit to the clerks certificates on petitions for review of orders made by them, together with a statement of the questions presented, the *findings,* and orders thereon, the petition for review, a transcript of the evidence or a summary thereof, and all exhibits."

This finding that appellant and Leroy actually bid in the entire amount of their respective lien claims at the sale of September 6, 1957, could not be reversed by the District Court unless clearly erroneous.

General Bankruptcy Order 47.

However, the referee's order was subject to control of the District Court, except only as to vested rights which may have accrued under it, and could be corrected if found to be erroneous or modified to suit the facts or vacated and set aside.

11 U. S. C. A., Sec. 11(a)(10);

General Bankruptcy Order 47.

In re Sparta Canning Co., 73 F. 2d 732, 733 (7th Cir., 1934);

2 Remington on Bankruptcy (6th Ed.) 579.

Accordingly, since the referee found that appellant and Leroy had utilized the entire amount of their lien claims upon their bid but did nothing about appellant's chattel mortgage of record, the District Court had the right to order appellant to release said chattel mortgage. Thus, the ruling of the District Court was proper.

B. Appellant's Arguments Do Not Warrant Reversal of the District Court's Order.

Appellant makes the following arguments in its opening brief in support of its contention that its lien claim and chattel mortgage were not satisfied nor extinguished by the bid and sale:

First, appellant urges that the referee improperly found in its certificate on review that appellant and Leroy had utilized the value of their lien claims upon the sale and bid and also that no such finding was made. (Appellant's Op. Br. pp. 56-58.)

In support of this contention, appellant cites *In re Peoria Braumeister Co.,* 138 F. 2d 520 (7th Cir., 1943). However, there the referee attempted to change formal findings in his certificate on review. In the instant action, there were no formal findings except as set forth in the referee's certificate on review. Moreover, in *Peoria Braumeister,* appellant made a motion to strike the petition for review directed to the District Court. Appellant did not make such motion in the instant action.

Finally, the finding by the referee in the instant case was in accordance with Section 39(a)(8) of the Bankruptcy Act, 11 U. S. C. A. Section 67(a)(8), and with General Bankruptcy Order 47.

Second, appellant urges that the recital in the bid that the real property was acquired subject to the liens of appellant and Leroy established as a matter of law that there was no intention to merge the mortgage with the fee. (Appellant's Op. Br. pp. 59-60.)

However, appellant ignores the rule of law that merger is a question of intent and that intent is a question of

fact; that the form of the bid does not control its substance and is at best an indicia of intent.

Moreover, the cases cited by appellant do not support its position. In *Anglo California Bank v. Field,* 146 Cal. 644, 652 (1905), the court determined that there was no intent to merge as a matter of fact. *Monheit v. Cigna,* 28 Cal. 2d 19 (1942), involved a tax lien and is not apposite to the question involved in the instant case.

In *Philadelphia Savings Fund Society v. Stern,* 23 A. 2d 413 (1942), cited by appellant, the court held on page 415 as follows:

> ". . . a mortgagee's acquisition of title to mortgaged property by a conveyance under and subject to the mortgage does not operate *automatically and inexorably* to extinguish the personal liability to the mortgagor for the debt secured. *Whether or not it has such an effect depends upon the intention of the parties to the conveyance. . . .*"

Thus, merely because the bid stated that it was subject to the liens of appellant and Leroy did not of itself prevent a merger in this case, as it is overall intent which governs.

Third, appellant next argues that a merger does not result from a conveyance or transfer of the equity of redemption to an agent or trustee of the mortgagee. Thus, appellant urges since the bid was in the name of S. Kohn, there could be no merger. (Appellant's Op. Br. pp. 60-63.)

However, all of the cases cited by appellant are based upon the premise that the intention of the parties controls whether there was a merger, and that one of the elements of intention is whether title was taken in the name of an agent or trustee. In the principal cases relied upon by

appellant, the record established a relationship of agent or trustee. There is no such relationship established in the instant action which unequivocably shows that the bid was in fact that of appellant and Leroy, but made only for convenience in the name of S. Kohn, a secretary of the attorney for said bidders. [R. pp. 110-111, 117-118, 121-122.] Moreover, both the referee and the District Court found an intent to merge.

Finally, appellant urges the theory of intervening liens in support of its position that a merger did not take place. (Appellant's Op. Br. pp. 63-65.)

Although appellant asserts the intervening lien theory, it does not cite any case involving facts similar to those of the instant action. The principal assets of the bankrupt were the land and the Hotel Moulin Rouge. There were no intervening liens on said assets which could prejudice appellant upon any merger, because the sale was free and clear of all liens. Thus, with reference to the principal assets acquired by the sale, there could have been no objection to a merger and neither appellant nor Leroy interposed any such objection, nor have they filed any petitions for review of the referee's orders thereon.

Finally, even if there were intervening liens, this would be only one element of intent. The bid could have provided that merger was not intended. The implied finding of the referee and the District Court was that a merger took place. The facts clearly support such a finding.

II.

The District Court Had Jurisdiction to Order Appellant to Release Its Chattel Mortgage Through Escrow.

A. The District Court Properly Modified the Referee's Order.

Appellant has raised a number of procedural points in its appeal, relating to the insufficiency of appellee's petition for review, her right to review and the power of the District Court to determine an independent controversy between the parties to this appeal.

However, none of these procedural questions have any bearing upon this appeal.

On September 6, 1957, the referee ruled that appellant's lien was valid. Appellant bid in the amount of said lien to purchase the real property of bankrupt. [R. 37-44.] On September 23, 1957, the sale to appellant and Leroy was confirmed by the referee. [R. 66-75.] Appellee filed her petitions for review of both orders of the referee.

At the hearing on appellee's petitions for review before the District Court, it was argued that the lien claim of appellant had been satisfied in full by utilizing the amount of said claim in bidding on the real property at the sale of September 6, 1957. Thus, it was urged that since appellant was entitled to only one satisfaction, it had no further claim under its chattel mortgage. [R. 124-127.]

Although the District Court specifically dismissed appellee's petitions for review, denied her the relief sought under said petitions and overruled all of her objections to the referee's orders, it nevertheless modified the referee's order of September 23, 1957, and ordered appellant to

deposit a release of its chattel mortgage in the escrow opened for purchase of the bankrupt's real property. [R. 135-136.]

Appellant cites no authority and makes no argument in its opening brief that the District Court did not have jurisdiction to modify said referee's order.

It is clear that under Bankruptcy Act, Section 2(10), 11 U. S. C. A., Section 11(10), the District Court had the right and power to

> "consider and confirm, modify or overrule, or return, with instructions for further proceedings, records and findings certified"

by the referee.

Moreover, under Section 2(2) of the Bankruptcy Act, 11 U. S. C. A., Section 11(2), the District Court was given the power to:

> "allow claims, disallow claims, reconsider allowed or disallowed claims, and allow or disallow them against bankrupt estates."

Furthermore, under Section 57(k) of the Bankruptcy Act, 11 U. S. C. A., Section 93(k),

> "claims which have been allowed may be reconsidered for cause and reallowed or rejected in whole or in part according to the equities of the case. . . ."

In 8 Remington on Bankruptcy (6th Ed.) 295, it is stated, that:

> "Regardless of the right to demand review of a referee's order, *it is thoroughly established that the district judge can proceed to review such orders on his own initiative if he sees fit to do so;* therefore, it is immaterial whether the judge has a clear right

> to review or not, if the judge sees fit to entertain the application. This power stems from the inherent power of the court and from Sec. 2(a)(10) of the Bankruptcy Act. . . ."

In 2 Remington on Bankruptcy (6th Ed.) 579, it is stated that:

> "As to scope of review, the judge in reviewing an order of the referee, is not confined to a consideration of the latter's certificate but may consider any point presented by the record."

In *Evarts v. Eloy Gin Corp.,* 204 F. 2d 712, 716 (9th Cir., 1953), cited by appellant in its opening brief, the court stated that the bankruptcy court has summary jurisdiction in

> ". . . all matters of administration, such as allowance, rejection and reconsideration of claims . . . determination of the preferences and priorities to be accorded to claims presented for allowance and payment in regular course. . . ."

In *Columbia Gas & Electric Corp. v. United States,* 153 F. 2d 101 (6th Cir., 1946), *cert. den.* 329 U. S. 737, the court stated on page 101 that the Supreme Court has

> ". . . recognized also that the equity powers of the bankruptcy court may be exerted to subordinate the claims of one claimant to those of others of the same class *where its conduct in acquiring or asserting its claim is contrary to established equitable principles.*"

Thus, it is manifestly clear that the District Court possessed the inherent power to determine that appellant had received full satisfaction of its claim, that it was equitable that it be satisfied only once, and that it had no further right to retain its chattel mortgage of record, which was formerly additional security for the same claim.

However, appellant urges on pages 46-51 and 66-71 of its opening brief that the District Court had no jurisdiction to determine rights and priorities between appellant and appellee regarding their respective chattel mortgages.

It is true that ordinarily the District Court does not take jurisdiction in controversies between two persons over a matter in which the trustee in bankruptcy has no interest. There is an exception in cases involving reorganizations.

> *In re Burton Coal Company,* 126 F. 2d 447, 448 (7th Cir., 1942).

However, in *Pepper v. Litton,* 308 U. S. 295 (1939), the court stated on pages 304 and 305 as follows:

> "By virtue of Section 2, a bankruptcy court is a court of equity at least in the sense that in the exercise of the jurisdiction conferred upon it by the act, it applies the principles and rules of equity jurisprudence . . . *among the granted powers are the allowance and disallowance of claims;* the collection and distribution of the estates of bankrupts and the determination of controversies in relation thereto; *the rejection in whole or in part 'according to the equities of the case' of claims previously allowed* . . . in such respects the jurisdiction of the bankruptcy court is exclusive of all other courts. . . ."
>
> "The bankruptcy courts have exercised these equitable powers in passing on a wide range of problems arising out of the administration of bankrupt estates. *They have been invoked to the end that fraud will not prevail, that substance will not give way to form, that technical considerations will not prevent substantial justice from being done.* By rea-

son of the express provisions of Section 2, these equitable powers are to be exercised on the allowance of claims, . . ."

Bank of America v. Erickson, 117 F. 2d 796 (9th Cir., 1941), decided by this court is directly in point. There, cerain creditors entered into an agreement to subordinate their claims. The trustee in bankruptcy objected to allowing the claim of said creditors on a parity with the general creditors, because of said subordination. The referee ordered the claims subordinated. Appellant argued that there was a justiciable controversy growing out of the agreement to subordinate between it and the other creditors, that the bankruptcy court was without jurisdiction to determine the dispute, and that the matter should be heard in another forum. The court stated on page 798 as follows:

> "The argument finds little support in the authorities. *The bankruptcy court has undoubted power to subordinate a general claim to other claims in the same category where for any reason, legal or equitable it ought to be subordinated."*

See also:

Heiser v. Woodruff, 327 U. S. 726 (1945);

Wheeling Valley Coal Corp. v. Mead, 171 F. 2d 916 (4th Cir., 1949);

Woodruff v. Heiser, 150 F. 2d 873 (10th Cir., 1945), cert. den. 326 U. S. 778;

In re International Power Securities Corp., 170 F. 2d 399 (3rd Cir., 1948).

In the instant action, the District Court did not rule that appellee's chattel mortgage was valid and subsisting nor did it decide a controversy between appellant and

appellee. It merely ordered that appellant deposit a release of its chattel mortgage in escrow, thus, impliedly holding that appellant's lien claim had been fully satisfied by virtue of its bid at the sale of September 6, 1957. Moreover, the District Court specifically ordered that the release of appellant's chattel mortgage was *without prejudice to its right to interpose all claims and defenses to appellee's chattel mortgage,* except the defense of priority. Of course, since the District Court found that appellant's lien claim had been satisfied, the chattel mortgage had no further priority. [R. 135-136.]

The District Court did not decide a controversy between appellant and appellee. It determined in the exercise of its proper jurisdiction to allow, disallow, reject or subordinate claims, that appellant's lien claim had been satisfied and thus should be released. Appellant has offered no authority holding that such a ruling was beyond the District Court's power.

B. The Appellant's Procedural Arguments Do Not Warrant Reversal of the District Court's Order.

However, even if the District Court had granted appellee's petitions for review, the procedural arguments raised by appellant would not warrant reversal of the order:

First, appellant argues on pages 36-39 of its opening brief that appellee was not a person aggrieved, and had no right to seek review of the referee's order because the sale of the personal property was subject to chattel mortgages and conditional sales contracts.

Section 39(c) of the Bankruptcy Act, 11 U. S. C. A., Sec. 67, grants the right to review referee's order to "a person aggrieved." The act does not define who are aggrieved persons.

However, in *Rogers v. Bank of America,* 142 F. 2d 128 (9th Cir., 1944), cited by appellant, this Court defines who is *not* aggrieved. The Court stated on page 129 as follows:

> "The bank has filed no claim in the bankruptcy proceedings; it does not occupy the status of a creditor or lienor. It is a stranger to those proceedings and therefor cannot be considered a 'person aggrieved.' "

It is obvious that the *Rogers* case is not authority for appellant's position in the instant action because appellee was a creditor of the bankrupt and also a lienor, by virtue of her chattel mortgage. [R. 21-29.] Moreover, in none of the cases cited by appellant, is the factual situation analogous to the instant proceedings. Here, the failure of the referee to provide in his order that appellant's chattel mortgage was extinguished, clearly imposed a burden upon appellee, diminished her property and detrimentally affected her claim.

The court, in *In re Camp Packing Co.,* 146 Fed. Supp. 935, 938 (N. D. N. Y., 1956), also cited by appellant in its opening brief, held a secured creditor was an aggrieved person, and stated as follows on page 938:

> "Reported decisions do not seem to contain an all inclusive definition of the term 'a party aggrieved' as used in the applicable statute . . . it would seem that a review is authorized if the party petitioning for same shows that *his property may be diminished, his burdens increased or his rights detrimentally affected by the order sought to be reviewed.* . . ."

Because of the merger in this proceeding, the failure of the referee to extinguish appellant's chattel mortgage

detrimentally affected appellee's rights and made her aggrieved.

Second, appellant urges on pages 40-43 of its opening brief, that appellee is estopped to review the referee's order.

The referee's certificate on review set forth that appellee was estopped to petition for review. [R. 120.]

However, estoppel is generally a question of fact.

Quon v. Niagara Fire Insurance Co., 190 F. 2d 257 (9th Cir., 1951);

Parke v. Franciscus, 194 Cal. 284, 297 (1924);

18 *Cal. Jur.* 2d 413.

Thus, had the District Court found that appellee was not estopped, it would have ruled upon a factual question, which this court would not disturb on appeal. Appellant has cited no cases where the Court of Appeals has reversed a District Court finding of no estoppel.

Moreover, appellee should not be estopped because she *did* present her contentions prior to the referee's order of September 23, 1957, confirming the sale. Appellee's position was presented to the referee by her petition for review of the order of September 6, 1957. [R. 50-56.] This was rejected by the referee. [R. 66-75.] Thus, appellee should not be estopped.

Third, appellant asserts on pages 43-45 of its opening brief that appellee's petition for review was insufficient.

However, the District Court had the inherent power to grant appellee's petition, even if it was defective.

Bankruptcy Act, Sec. 2(a)(10), 11 U. S. C. A., Sec. 11(a)(10);

In re Moscovitz, 63 Fed. Supp. 1000 (W. D. Ky., 1946);

In re Florsheim, 24 Fed. Supp. 991 (S. D. Cal., 1938), app. dism'd 110 F. 2d 660 (9th Cir., 1940);

8 Remington on Bankruptcy (6th Ed.), 295;

2 Collier on Bankruptcy (14th Ed.), 1479.

In the *Florsheim* case, the court stated on page 992 that:

> "where a petition for review is clearly erroneous . . . *the court may decide to pass upon points not specifically designated* . . . or it may dismiss the petition."

Thus, even if defective, the District Court clearly could have ruled upon appellee's petition. Appellant has cited no case where an Appellate Court has reversed the District Court after it had considered a defective petition for review.

Conclusion.

The order of the District Court should be affirmed.

Respectfully submitted,

ARTHUR N. GREENBERG,

Attorney for Appellee.